(1)

88-558

No. _____

Supreme Court, U.S.
FILED
SEP 24 1988
JOSEPH F. SPANIOL, JR.
CLERK

IN THE

Supreme Court of the United States

October Term, 1988

MARGARETHA WALK, an individual, and MAURICE WALK, Trustees for the Cynthia Walk Trust, the Dinand M. Walk Trust, and the Margaretha Walk Trust and VINCENT CIARLANTE,

Petitioners,

vs.

THE BALTIMORE AND OHIO RAILROAD, CHESAPEAKE AND OHIO RAILROAD and THE CSX CORPORATION,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

MICHAEL P. MALAKOFF
ELLEN M. DOYLE
BERGER, KAPETAN, MALAKOFF
& MEYERS, P.C.
508 Law and Finance Building
Pittsburgh, Pennsylvania 15219
(412) 281-4200
Attorneys for the Petitioners-Plaintiffs

Batavia Times Publishing Co.
Harold L. Berkoben
Pittsburgh, Pa. (412) 881-7463

Questions Presented

1. Whether a series of episodes of criminal activity spanning a ten year period involving thousands of investors in four different corporations constitutes only one RICO scheme which is not a sufficient pattern of racketeering activity within the meaning of RICO?

2. Whether the Fourth Circuit's requirement that the RICO conduct alleged also "pose a special threat to social well-being" is unconstitutionally vague?

TABLE OF CONTENTS.

	Page
Questions Presented	i
Table of Contents	ii
Table of Authorities	iii
Statement of Jurisdiction	1
Statute Involved	2
Statement of the Case	3
Reasons for Granting the Writ	7
1. This Honorable Court has already recognized the need to resolve the differences existing among the Courts of Appeals with respect to RICO's pattern requirement	7
2. The Fourth Circuit's attempt to distinguish between racketeering activities on the basis of its personal, undefined notions as to what activities "Pose A Special Threat To Social Well-Being" creates an unconstitutionally vague standard of conduct	10
Conclusion	15
Appendices:	
Appendix A—Text of Sections 1961(1), 1961(5), 1962(a), and 1962(c) of the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §1961 *et seq.*	A1
Appendix B—Opinion of the United States District Court for the District of Maryland (1987)	A3
Appendix C—Opinion of the United States Court of Appeals for the Fourth Circuit (1988)	A10

Page

TABLE OF AUTHORITIES.

Bank of America v. Touche Ross & Co., 782 F.2d 966 (11th Cir. 1986) 9
Barticheck v. Fidelity Union Bank/First Nat. State, 832 F.2d 36 (3d Cir. 1987) 9
Beck v. Manufacturers Hanover Trust Company, 820 F.2d 46 (2d Cir. 1987), *cert. denied*, 108 S.Ct. 698 (1988) 13
H.J. Inc. v. Northwestern Bell Telephone Company, 829 F.2d 648 (8th Cir. 1987), *cert. granted*, 108 S.Ct. 1219 (March 21, 1988) (No. 87-1252) 7,8,9
International Data Bank v. Zepkin, 812 F.2d 149 (4th Cir. 1987) 10
Lanzetta v. New Jersey, 306 U.S. 451 (1939) 12
Liquid Air Corp. v. Rogers, 834 F.2d 1297 (7th Cir. 1987), Petition for Certiorari pending at No. 87-1262 8
Lockspeiser v. Western Maryland Company, 768 F.2d 558 (4th Cir. 1985) 4
Pittsburgh Terminal Corporation v. .Baltimore & Ohio R. Co., 680 F.2d 933 (3d Cir.), *cert. denied*, 457 U.S. 1056 (1982) 3
Sedima, S.P.R.L. v. Imrex Co., 473 U.S. 479 (1985) 10,12
United States v. Boyer, 694 F.2d 58 (3d Cir. 1982) 13
United States v. Carter, 493 F.2d 704 (2d Cir. 1974) 11
United States v. Griffin, 660 F.2d 996 (4th Cir. 1981) 13
United States v. Ianniello, 808 F.2d 184 (2d Cir. 1986) 13

Page

United States v. Tillett, 763 F.2d 628 (4th Cir. 1985) 13
Walk v. B&O Railroad Co., 659 F.Supp. 824 (D.Md. 1987), *aff'd.* 847 F.2d 1100 (4th Cir. 1988) 4,8
Yellow Bus Lines, Inc. v. Local Union 639, 839 F.2d 782 (D.C. Cir. 1988) 9

IN THE

Supreme Court of the United States

October Term, 1988

No. _____

MARGARETHA WALK, an individual, and MAURICE WALK, Trustees for the Cynthia Walk Trust, the Dinand M. Walk Trust, and the Margaretha Walk Trust, and VINCENT CIARLANTE,

Petitioners,

vs.

THE BALTIMORE AND OHIO RAILROAD, CHESAPEAKE AND OHIO RAILROAD, and THE CSX CORPORATION,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

Statement of Jurisdiction

Jurisdiction in the District Court was based on 18 U.S.C. §1964(a) and on diversity of citizenship under 18 U.S.C. §1332. Jurisdiction in the Court of Appeals for the Fourth Circuit was based on 28 U.S.C. §1291 because the dismissal of the Complaint constituted a final and appealable order.

The jurisdiction of this Court to review the judgment of the Fourth Circuit is invoked under 28 U.S.C. §1254(1).

Statute Involved

The text of sections 1961(1), 1961(5), 1962(a), and 1962(c) of the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §1961 *et seq.* is reprinted in the Appendix and designated Appendix A.

Statement of the Case

Margaretha and Maurice Walk, as trustees, and Vincent Ciarlante [hereafter collectively referred to as "Walks"], and other minority shareholders of the Baltimore & Ohio Railroad ["B&O"] filed a class action against CSX Corporation and other affiliated corporations ["CSX"] alleging a series of mail fraud and securities fraud transactions spanning a period of ten years taken by CSX against various minority equity holders of its subsidiary corporations.

The *first* scheme was executed on December 13, 1977 and involved the transfer of the majority of the B&O's non-rail assets, including vast real estate holdings, into a shell subsidiary corporation, and the declaration on that same day of a dividend in kind of the subsidiary's stock to the holders of B&O's common stock, without any notice to the B&O's convertible debentureholders. The first scheme described in Walks' Complaint ["Scheme One"] has already been found to be a securities violation directed against hundreds of investors. See generally *Pittsburgh Terminal Corporation v. Baltimore & Ohio R. Co.*, 680 F.2d 933, 943 (3d Cir.), *cert. denied*, 457 U.S. 1056 (1982).

The *second* scheme involved a 1983 merger of one of B&O's major operating railroads, the Western Maryland Railway ["WMR"], into a wholly owned subsidiary of CSX, thereby eliminating all minority shareholder interests in the WMR.

The *third* scheme involved a 1983 merger of the Western Maryland Company ["WMC"], which had no employees and no operations, but owned valuable assets, into another CSX wholly owned subsidiary, thereby eliminating all minority interests in the WMC. A court of appeals suggested that Scheme Three set forth a

violation of the Exchange Act. See *Lockspeiser v. Western Maryland Company*, 768 F.2d 558, 561 (4th Cir. 1985).

The *fourth* scheme involved the elimination of all of the minority shareholder interests in the B&O in a 1987 merger of B&O into another of CSX' wholly owned subsidiaries.

The Walks' Amended Complaint alleged numerous criminal acts of mail fraud and securities fraud by CSX and its affiliates in carrying out the four schemes. The District Court (659 F.Supp. 824 (D.Md. 1987)) found the two RICO counts of Walks' Amended Complaint deficient in four respects:

1. The Complaint failed "to characterize the defendants as persons who regularly commit federally indictable fraud." *Id.* at 825.

2. The Complaint failed to characterize "the railroad defendants as persons whose criminal conduct poses a 'special threat to social well-being.' " Id.

3. "Despite plaintiffs' counsel's ingenuity in identifying multiple fraudulent 'schemes,' . . . there is but one real 'scheme' alleged in this case." *Id.*, and

4. The Complaint "involves ordinary claims of fraud . . . which are best left to state law." *Id.*

The Court of Appeals for the Fourth Circuit affirmed the dismissal (847 F.2d 1100 (4th Cir. 1988)) finding that the Walks had failed to satisfy the pattern of racketeering activity requirement of Sections 1962(a) and (c). *Id.* at 1102. The Fourth Circuit recognized that the RICO issue it was deciding had "bitterly divided the circuits":

> As *Zepkin* and the cases following it illustrate, it is the continuity aspect of *Sedima's* pattern analysis which has given us the greatest difficulty in application. We are not alone in this regard—the proper application of the continuity prong has bitterly divided the circuits. *Id.* at 1103.

The Fourth Circuit admitted its own difficulty in articulating a standard for the pattern of racketeering requirement:

> Since *Sedima*, the lower courts have struggled to give content to the vague notions of 'continuity' and 'relationship that are now considered the distinctive characteristics of the RICO 'pattern.' . . . this task has not been an easy one, for the terms 'relationship' and 'continuity,' as used in *Sedima*, are inherently contradictory. 'Relationship implies that the predicate acts were committed close together in time, involve the same victim or type of misconduct, or both; 'continuity' implies more extended periods of time almost inevitably involving different victims. *Id.* at 1003.

The Fourth Circuit, stating that the Walks' claims present the "closest question yet", found that the Walks had failed to state a claim for relief under RICO because they had not properly alleged a pattern of racketeering activity even though "the predicate acts alleged here span a period of ten years and can be grouped into several distinct 'episodes' of activity, each of which is arguably self-contained." *Id.* at 1104-05.

The Fourth Circuit distinguished between the securities and mail fraud schemes alleged by the Walks and schemes involving other kinds of predicate acts, which it considered to be of a more serious criminal dimension:

> [T]he objective of the related predicate acts is a factor to be considered in assessing the criminal dimension and degree. In this case, that objective is sufficiently limited that we cannot say the related predicate acts suggest ongoing criminal activity of sufficient scope and persistence to pose a special threat to social well-being. *Id.* at 1005.

The Walks filed a petition for rehearing *en banc* to request the entire Court of Appeals to resolve the conflict between the holding of the Panel and the holdings of the majority of the other Courts of Appeals, which was denied by the Fourth Circuit on June 30, 1988.

REASONS FOR GRANTING THE WRIT

1. This Honorable Court has already recognized the need to resolve the differences existing among the Courts of Appeals with respect to RICO's pattern requirement.

On March 24, 1988, this Court granted certiorari in *H.J. Inc. v. Northwestern Bell Telephone Company*, 829 F.2d 648 (8th Cir. 1987), *cert. granted*, 108 S.Ct. 1219 (March 21, 1988) (No. 87-1252), in order to review the opinion of the Court of Appeals for the Eighth Circuit dismissing a complaint for failure to allege the "pattern of racketeering activity" requirement of RICO. The Eighth Circuit requires that, in addition to the predicate offenses being alleged, there must be a claim that the predicate offenses constitute multiple schemes and that there is criminal activity other than that relevant to the RICO case being brought.

Other Courts of Appeals have disagreed with the Eighth Circuit's grafting of a multiple scheme requirement onto RICO's pattern requirement, but have disagreed among themselves as to what constitutes a pattern. The Seventh Circuit, for example, attempted to develop a list of factors to be considered in determining whether such a pattern existed:

> Relevant factors include the number and variety of predicate acts and the length of time over which they were committed, the number of victims, the presence of separate schemes and the occurrence of distinct injuries. *Morgan v. Bank of Waukegan*, 804 F.2d 970, 975 (7th Cir. 1986).

The Third Circuit also attempted to objectify the analysis of the pattern requirement:

> [T]he existence of a RICO pattern does not turn on the abstract characterization of racketeering acts as 'continuous' and 'related' but rather on a combination of specific factors such as the number of unlawful acts, the length of time over which the acts were committed, the similarity of the acts, the number of victims, the number of perpetrators, and the character of the unlawful activity. *Barticheck v. Fidelity Union Bank/First Nat. State,* 832 F.2d 36, 39 (3d Cir. 1987).

The Fourth Circuit has rejected any attempt to analyze specific factors in determining the existence of a pattern of racketeering activity. In *Walk,* 847 F.2d at 1104, it stated:

> We did not attempt to identify a range of factors relevant to the continuity inquiry as had the Seventh Circuit in *Morgan,* but we did indicate that the inquiry ought to focus on whether the related predicate acts suggested 'ongoing unlawful activities whose scope and persistence pose a special threat to social well-being.' *Id.*

This Court's clarification of the pattern requirement in *H.J. Inc. v. Northwestern Bell Telephone Company,* may or will resolve the RICO issue presented by this Petition.

It is clear that under the standards articulated for pleading a pattern of racketeering injury in the Third and Seventh Circuits, the Walks' Complaint would not have been dismissed.

The Walks' claims, which were dismissed by the Fourth Circuit, involved more victims, more injuries, more perpetrators and more predicate acts spanning a greater period of time than the pattern of racketeering activity found sufficient by the Seventh Circuit in *Liquid Air Corp. v. Rogers,* 834 F.2d 1297 (7th Cir. 1987) (petition for certiorari filed at No. 87-1262), where that Court stated:

> Therefore, we have a single scheme which lasted seven months and defrauded a single victim. The defendants committed nineteen separate acts, each resulting in use of the mails and use of the wire service. Each time an invoice was falsely prepared, it deprived Liquid Air of its entitlement to rent or replacement value. Therefore, each act resulted in a distinct injury to Liquid Air and a concomitant benefit to D&R. We find that the repeated infliction of economic injury upon a single victim of a single scheme is sufficient to establish a pattern of racketeering activity for purposes of civil RICO. *Id.* at 1304.

See also the following cases where other Courts of Appeals found substantially lesser allegations of racketeering activity to be sufficient to state a claim under RICO: *Barticheck v. Fidelity Union Bank/First Nat. State,* 832 F.2d 36 (3d Cir. 1987) (more than two predicate acts, involving twenty-three investors in a limited partnership scheme); *Yellow Bus Lines, Inc. v. Local Union 639,* 839 F.2d 782, 788-89 (D.C. Cir. 1988) (petition for certiorari filed 88-190) (ten predicate acts, one victim, one scheme); and *Bank of America v. Touche Ross & Co.,* 782 F.2d 966, 970-71 (11th Cir. 1986) (9 predicate acts, 5 victims, 1 scheme).

It is respectfully submitted that this Court should grant the Walks' Petition for Certiorari, and consider their appeal or stay the appeal pending this Court's review of the conflict among the Courts of Appeals as to the requirements of RICO's pattern of racketeering activity in *H.J. Inc. v. Northwestern Bell Telephone Company, supra.*

2. The Fourth Circuit's attempt to distinguish between racketeering activities on the basis of its personal, undefined notions as to what activities "Pose A Special Threat To Social Well-Being" creates an unconstitutionally vague standard of conduct.

The Fourth Circuit has been exceedingly reluctant to accept this Court's decision in *Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479 (1985) and to permit civil RICO claims to proceed.

Clearly the Fourth Circuit is dissatisfied with the Congressional inclusion of mail fraud, wire fraud and securities fraud in the predicate acts chosen by Congress in §1961(1) of RICO. In its opinion in this case, it distinguished between white-collar mail or securities fraud schemes and what it perceived to be more serious criminal schemes:

> Virtually every action taken by a controlling majority in the course of its stewardship of a corporation is subject to challenge as either mail or securities fraud. To hold indiscriminately that proof of several such acts occurring over the course of a period of years constitutes a RICO pattern would be to make the statute's extraordinary penalties available to virtually every disgruntled minority shareholder harmed in the process. Such a result would not only have a chilling effect on the transaction of legitimate corporate business, but also sanction a use of the RICO statute that we do not think Congress intended. *Id.* at 1105.

See also the Fourth Circuit's discussion in the opinion below of its prior decision in *International Data Bank v. Zepkin*, 812 F.2d 149 (4th Cir. 1987):

> In *Zepkin* . . . we recognized that a 'single, limited scheme' designed to perpetrate a single fraud should not be transformed into a RICO violation simply

> because the fraud's commission required several acts of mail or wire fraud; such an interpretation would, we thought, virtually read the pattern requirement out of the statute for it is 'the unusual fraud that does not enlist the mails and wires in its service at least twice.' *Id.* at 1104 (citation omitted).

In order to avoid what it feared to be abusive use of RICO against legitimate businesses, and those associated with legitimate businesses, the Fourth Circuit requires that the RICO scheme alleged must "pose a special threat to social well-being." *Id.* at 1105. The Fourth Circuit has not yet reviewed a scheme in a civil RICO action which poses such a special threat to social well-being, since it has not upheld the sufficiency of a single civil RICO complaint, but it has suggested that "a scheme that contemplates a repeated infliction of independent economic injuries—e.g., a series of bank robberies or embezzlements", might satisfy its standard. *Id.* at 1106.

In the Fourth Circuit, the usual mail or wire frauds committed by ordinary white-collar criminals do not appear to be actionable in civil RICO proceedings. *Id.* at 1104. Contrast *United States v. Carter,* 493 F.2d 704 (2d Cir. 1974):

> The fact that the alleged perpetrators are presumably respected and entrusted with responsibility . . . by stockholders does not suggest . . . that they are incapable of engaging in organized criminal activity. We all stand equal before the bar of criminal justice, and the wearing of a white collar, even though it is starched, does not preclude the organized pursuit of unlawful profit. *Id.* at 708.

The Fourth Circuit's dissatisfaction with the scope of RICO is inconsistent with the statute's scope as drafted. Congress fully appreciated the breadth of RICO's civil provisions. In a law review article by Senator McClellan

(a sponsor of and chair of the subcommittee which wrote the statute) he stated:

> It is impossible to draw an effective statute which reaches most of the commercial activity of organized crime, yet does not include offenses commonly committed by persons outside of organized crime as well. McClellan, *The Organized Crime Act (S. 30) or its Critics: Which Threatens Civil Liberties?*, 46 Notre Dame L.Rev. 55, 143-44 (1970).

The Fourth Circuit's engrafting of an additional requirement onto RICO's pattern requirement is inconsistent with *Sedima*, which rejected any judicial amendment of RICO to add amorphous requirements designed at limiting the application of RICO, 473 U.S. at 500, and creates a standard which is unconstitutionally vague. This Court has long recognized the need for criminal statutes to provide reasonable notice of the conduct which they proscribe:

> That the terms of a penal statute creating a new offense must be sufficiently explicit to inform those who are subject to it what conduct on their part will render them liable to its penalties is a well-recognized requirement, consonant alike with ordinary notions of fair play and the settled rules of law; and a statute which either forbids or requires the doing of an act in terms so vague that men of common intelligence must necessarily guess at its meaning and differ as to its application violates the first essential of due process of law. *Connally v. General Constr. Co.*, 269 U.S. 385, 391 (1926).

See also *Lanzetta v. New Jersey*, 306 U.S. 451 (1939), where this Court found unconstitutionally vague a statute penalizing "gangsters."

RICO contains both criminal and civil provisions, which require a uniform interpretation. The pattern of racketeering activity requirement contained in 18 U.S.C. §§1962(a) and (c), applies equally to RICO's criminal provisions. See *Beck v. Manufacturers Hanover Trust Company*, 820 F.2d 46 (2d Cir. 1987), *cert. denied*, 108 S.Ct. 698 (1988), where the Second Circuit applied its criminal RICO requirements developed in *United States v. Ianniello*, 808 F.2d 184 (2d Cir. 1986), to a civil RICO complaint. See also *United States v. Boyer*, 694 F.2d 58 (3d Cir. 1982), where the Third Circuit stated:

> The standard of proof for civil liability in fraud is lower than the proof beyond a reasonable doubt required for a criminal conviction. But there is no reason to suppose that in enacting criminal statutes prohibiting mail fraud or securities fraud the Congress intended that the substantive element of the offense—the scienter—should be different than for civil liability for fraud. *Id.* at 60.

The Fourth Circuit's announcement below that it will determine on a case by case basis whether "the related predicate acts suggest ongoing criminal activity of sufficient scope and persistence to pose a special threat to social well-being" renders RICO's pattern of racketeering requirement unconstitutional in its application. Significantly, the Fourth Circuit has failed to mention this requirement in its affirmance of criminal RICO convictions. *United States v. Griffin*, 660 F.2d 996 (4th Cir. 1981) and *United States v. Tillett*, 763 F.2d 628 (4th Cir. 1985). The standard provides no guidance to those whose conduct it seeks to prevent.

In fact, the purpose of the standard appears to be to permit the court to arbitrarily select from among those engaging in RICO predicate acts the defendants against whom the court will permit civil actions to be brought:

> The intent of Congress is not that RICO be used under all circumstances. Its intent is that RICO be used against racketeers, individuals who earn their livelihood through the repetitive and continuous commission of criminal acts. The statute, properly read, is not a "catch-all," but is instead a powerful tool to be used against racketeers and organized crime. Too frequently, this statute is used by attorneys against legitimate businesses. . . . *Gatoil (U.S.A.), Inc. v. Forest Hill State Bank*, No. 86-3579 (Unpublished). 6 RICO L.Rptr. 316, 321 (4th Cir. June 17, 1987).

This case provides yet another example where the Fourth Circuit is excluding those associated with "legitimate" businesses who violate the wire, mail and securities laws from the scope of RICO.

This Court should grant the Walks' petition for certiorari and reverse the Fourth Circuit's dismissal of the Walks' Complaint on the grounds that RICO's pattern of racketeering requirement does not additionally require a determination by a court that the conduct alleged poses "a special threat to social well-being."

Conclusion

For the reasons stated above, Petitioners Margaretha Walk, Maurice Walk, as Trustee, and Vincent Ciarlante, respectfully request this Honorable Court to grant their Petition for a Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit.

Respectfully submitted,

BERGER, KAPETAN, MALAKOFF
& MEYERS, P.C.
MICHAEL P. MALAKOFF
ELLEN M. DOYLE
508 Law & Finance Building
Pittsburgh, Pennsylvania 15219
(412) 281-4200
Attorneys for the Petitioners-Plaintiffs

Dated:

APPENDIX A

Text of Sections 1961(1), 1961(5), 1962(a), and 1362(c) of the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §1961 *et seq.*

§1961. Definitions

As used in this chapter—

(1) "racketeering activity" means . . . *** (B) any act which is indictable under any of the following provisions of title 18; . . . *** section 1341 (relating to mail fraud), section 1343 (relating to wire fraud),

* * *

(3) "person" includes any individual or entity capable of holding a legal or beneficial interest in property;

(4) "enterprise" includes any individual, partnership, corporation, association, or other legal entity, and any union or group of individuals associated in fact although not a legal entity;

(5) "pattern of racketeering activity" requires at least two acts of racketeering activity, one of which occurred after the effective date of this chapter and the last of which occurred within ten years (excluding any period of imprisonment) after the commission of a prior act of racketeering activity;

* * *

§1962. Prohibited activities

(a) It shall be unlawful for any person who has received any income derived, directly or indirectly, from a pattern of racketeering activity or through collection of an unlawful debt in which such person has participated as a principal within the meaning of section 2, title 18, United States Code, to use or invest, directly or indirectly, any part of such income, or the proceeds of

Appeal A—Text of Sections 1961(1), 1961(5), 1962(a), and 1962(c) of the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §1961 et seq.

such income, in acquisition of any interest in, or the establishment or operation of, any enterprise which is engaged in, or the activities of which affect, interstate or foreign commerce. . . . *** controlling or participating in the control of the issuer, or of assisting another to do so, shall not be unlawful under this subsection if the securities of the issuer held by the purchaser, the members of his immediate family, and his or their accomplices in any pattern or racketeering activity or the collection of an unlawful debt after such purchase do not amount in the aggregate to one percent of the outstanding securities of any one class, and do not confer, either in law or in fact, the power to elect one or more directors of the issuer.

* * *

(c) It shall be unlawful for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity or collection of unlawful debt.

* * *

APPENDIX B

Opinion of the United States District Court for the District of Maryland (1987)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MARYLAND

MARGARETHA WALK, an Individual, and MAURICE WALK, Trustees for the Cynthia Walk Trust, the Dinand M. Walk Trust, and the Margaretha Walk Trust, and VINCENT CIARLANTE,

v.

THE BALTIMORE AND OHIO RAILROAD, THE CHESAPEAKE AND OHIO RAILROAD and the CSX CORPORATION.

Civil No. S 87-488

John B. Isbister, Esq., Tydings & Rosenberg, of Baltimore, Maryland, and Michael P. Malakoff, Esq. and Ellen M. Doyle, Esq., Berger, Kapetan, Malakoff & Meyers, P.C., of Pittsburgh, Pennsylvania, for plaintiffs.

Richard Magid, Esq., Ward B. Coe, III, Esq., and William F. Ryan, Esq., Whiteford, Taylor & Preston, of Baltimore, Maryland, for defendants.

Smalkin, District Judge.

Filed: May 6th, 1987.

Appendix B—Opinion of the United States District Court for the District of Maryland (1987).

This is a three-count civil action before the Court on a pre-answer amended complaint, filed pursuant to 28 U.S.C. §§1331 and 1332, by minority shareholders of the B&O Railroad. (They seek class action status.) The first two counts claim civil violations of the Racketeer Influenced and Corrupt Organizations [RICO] statute, 18 U.S.C. §1961 *et seq.* The third count claims violation of a state-law based fiduciary duty owed to the minority B&O shareholders by the defendant C&O, and its parent CSX, as owners of the majority interest in B&O. The matter is now before the Court on the defendants' motion to dismiss the amended complaint, which has been briefed and opposed. No oral argument is necessary. Local Rule 6, D. Md.

The Court is convinced beyond a doubt, *see Conley v. Gibson*, 355 U.S. 41, 45-46 (1957), that this complaint fails to state a civil RICO claim under 18 U.S.C. §1962, because it does not allege, nor could it be further amended to allege, a legally sufficient "pattern of racketeering activity." Although the complaint recites a prolix catalogue of events and "schemes" going back many years (to 1977) and involving a number of persons and entities other than B&O minority shareholders, it shows no "pattern of racketeering activity" as that statutory RICO requirement has been interpreted in the Fourth Circuit. In *International Data Bank, Ltd. v. Zepkin*, 812 F.2d 149 (4th Cir. 1987), the Court stated that the "pattern of racketeering activity" requirement was intended to limit civil RICO to "those cases in which racketeering acts are committed in a manner characterizing the defendant as a person who regularly commits" certain crimes. Clearly, this complaint is

inadequate to characterize the defendants as persons who regularly commit federally indictable fraud. In fact, the discrete predicate acts of criminal fraud apparently alleged in this complaint include only certain activities pertaining to debenture holders in 1977, already the subject of another lawsuit, and the mailing of a supplemental brief in that lawsuit in 1982 (Amended Complaint, ¶¶32-36), the mailing of two proxy statements on March 18, 1983 (*Id.*, ¶¶40, 46), and the mailing of a press release and notice pertaining to the challenged merger. (*Id.*, ¶¶58, 61). As noted by the Supreme Court in *Sedima, S.P.R.L. v. Imrex Co., Inc.*, 105 S. Ct. 3275, 3285 n.19 (1985), two predicate criminal racketeering acts are necessary, but not sufficient, to make out a pattern of racketeering activity. In the Fourth Circuit, what suffices has been settled by *International Data Bank*:

> What constitutes a RICO pattern is thus a matter of criminal dimension and degree. To allow a "pattern of racketeering" to flow from a single, limited scheme such as this one would undermine Congress' intent that RICO serve as a weapon against ongoing unlawful activities whose scope and persistence pose a special threat to social well-being. The present case does not involve a "pattern of racketeering," but ordinary claims of fraud best left to "the state common law of frauds" and to "well-established federal remedial provisions."

812 F.2d at 155.

Despite plaintiffs' counsel's ingenuity in identifying multiple fraudulent "schemes," as portrayed in their dismissal opposition (filed May 5, 1987) at 3-4, there is but one real "scheme" alleged in this case, and that has to do with the valuation of minority shares and the

treatment of minority shareholders in the B&O. The carefully sifted sands through which plaintiffs have combed to find their "schemes" do not form any firm foundation for characterizing the railroad defendants as persons whose criminal conduct poses a "special threat to social well-being." *Id.* In short, this case involves ordinary claims of fraud, and no more, which are best left to state law. Thus, it fails to state a claim under RICO, and counts 1 and 2 will be dismissed by an order to be entered separately, for failure to state a claim upon which relief can be granted. Fed. R. Civ. P. 12(b)(6).

Count 3 alleges breach of fiduciary duty to minority shareholders, but it utterly fails to show any legally cognizable, timely-asserted injury to them short of the allegedly less-than-fair value presently being offered for their stock. The claims relating to the treatment of B&O minority shareholders arising from or at issue in the "PTC" litigation are clearly barred by limitations or are foreclosed by the judgment rendered March 31, 1987 by the United States District Court for the Northern District of Ohio in *Pittsburgh Terminal Corp. v. The Baltimore and Ohio Railroad, et al.*, Civil No. C 84-1267, a situation that plaintiffs' opposition does not address. This Court is of the opinion that the remaining claim in the third count, *viz.*, freeze-out of minority shareholders at an inadequate price (which is the only claim really at issue, *see, e.g.*, plaintiffs' opposition at 31, first full paragraph), is not cognizable under Maryland law as pleaded, because the plaintiffs can avail themselves of the remedy of appraisal, as provided in *Md. Corps. & Assn's Code Ann.* §§3-106 and 3-201—3-212 (1957, 1985 Repl. Vol.).

Appendix B—Opinion of the United States District Court for the District of Maryland (1987).

Although Judge Miller of this Court recognized that the sole minority shareholder of a Maryland corporation in a short-form merger might have a cause of action for breach of fiduciary duty in *very* limited circumstances, *Twenty Seven Trust v. Realty Growth Investors,* 633 F. Supp. 1028, 1037-9 (D. Md. 1982), he held that "inadequacy of price [offered for minority shares] alone does not warrant court intervention in corporate affairs." *Id.* at 1039, *citing Homer v. Crown, Cork & Seal Co.,* 155 Md. 66, 79-86, 141 A. 424, 431-34 (1928). *Homer* is still good law in Maryland. *See Lerner v. Lerner,* 306 Md. 771, 780-81 (1986). Here, inadequacy of the price being offered for the minority shares is the only *real* issue in Count III, and the non-statutory cause of action pleaded therein is not recognized in Maryland law. In the language of *Homer* itself, the question is whether, on a reading of the entire complaint, it appears to the court that "the fundamental issue thus made is not fraud but a debatable controversy over value. . . ." 155 Md. at 80. If fraud is not the fundamental issue, then, under *Homer,* the statutory appraisal is the exclusive remedy. A close reading of the amended complaint's attempted particularizations of "fraud" in connection with the merger, at ¶¶71-73, shows that these claims are no more than conclusory disagreements with income and asset valuations, stock valuations, and methods of accounting, which fall far short of establishing the requisite fraud under *Homer* to warrant an injunction against the merger. Looking at the individual allegations of fraud, the short-line sale contention of ¶71.a. does not, by itself or in conjunction with ¶67, adequately demonstrate the requisite fraud under *Homer,* because, *inter alia,* there is no allegation that the intention to sell short lines was in

fact *in esse* before the merger price was announced. The allegations of failure to make public projections of income and late reporting of income do not adequately plead the requisite fraud. (There is no duty to make public projections of income identified by plaintiffs under Maryland law.) Thus, ¶71.b. does not make out a sufficient case of fraud under *Homer.* Paragraph 72 attacks the integrity of the independent financial advisor, not of defendants, and there is no sufficient allegation of a duty on the part of defendants to make disclosures of Morgan Stanley's activities so as to make out a case of fraud under *Homer.* Whether taken alone or together, these attempted allegations of fraud convince the Court that fraud is not the essence of the plaintiffs' claim. Rather, here, as in *Homer,* the fundamental issue is inadequate price, and the few acts of "fraud" identified by plaintiffs are insufficient, as a matter of law, to make out together or separately the species of fraud required to be shown before a Maryland equity court will enjoin a short form or "cashout" merger. Because the statutory appraisal mechanism is not pleaded by plaintiffs here, and because it constitutes an adequate and exclusive remedy under Maryland law as applied to the facts of this case, plaintiffs' third claim also fails to state a claim upon which relief can be granted, Fed. R. Civ. P. 12(b)(6), and it, too, will be dismissed by the Order accompanying this Memorandum Opinion.

FREDERIC N. SMALKIN
United States District Judge

Appendix B—Opinion of the United States District Court for the District of Maryland (1987).

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MARYLAND

MARGARETHA WALK, an Individual, and MAURICE WALK, Trustees for the Cynthia Walk Trust, the Dinand M. Walk Trust, and the Margaretha Walk Trust, and VINCENT CIARLANTE,

v.

THE BALTIMORE AND OHIO RAILROAD, THE CHESAPEAKE AND OHIO RAILROAD and the CSX CORPORATION.

Civil No. S 87-488

ORDER

For the reasons stated in the foregoing Memorandum Opinion, IT IS, this 6th day of May, 1987, by the Court, ORDERED:

1. That plaintiffs' amended complaint BE, and the same hereby IS, DISMISSED, for failure to state a claim upon which relief can be granted; and

2. That the Clerk of Court mail copies of the foregoing Memorandum Opinion and of this Order to counsel for the parties.

FREDERIC N. SMALKIN
United States District Judge

APPENDIX C

Opinion of the United States Court of Appeals for the Fourth Circuit (1988)

PUBLISHED

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 87-3585

Margaretha Walk, an individual; Maurice Walk, Trustees for the Cynthia Walk Trust, the Dinand M. Walk Trust and the Margaretha Walk Trust; Vincent Ciarlante,

Plaintiffs-Appellants,

versus

The Baltimore and Ohio Railroad;
Chesapeake and Ohio Railroad;
The CSX Corporation,

Defendants-Appellees.

Appeal from the United States District Court for the District of Maryland, at Baltimore, Frederic N. Smalkin, District Judge. (CA-87-488-S)

Argued January 6, 1988. Decided May 31, 1988

Before WINTER, Chief Judge, and PHILLIPS and MURNAGHAN, Circuit Judges.

Appendix C—Opinion of the United States Court of Appeals for the Fourth Circuit (1988).

Ellen M. Doyle (Michael P. Malakoff; Berger, Kapetan, Malakoff & Meyers, P.C.; John B. Isbister; Tydings & Rosenberg on brief) for Appellants; Ward Baldwin Coe, III (Wilbur D. Preston, Jr.; Richard J. Magid,; William F. Ryan, Jr.; Whiteford, Taylor & Preston; Alan A. Rudnick, General Counsel, CSX Corporation on brief) for Appellees.

PHILLIPS, Circuit Judge:

Following the announcement by CSX Corp. (CSX) of a statutory short-form merger of one of its subsidiaries, the Baltimore & Ohio Railroad (B&O), into another, the Chesapeake & Ohio Railroad (C&O), appellants Margaretha Walk, Maurice Walk, and Vincent Ciarlante (the plaintiffs), as representatives of a putative class of minority shareholders in B&O, brought this action challenging the merger. The complaint, which named as defendants B&O, C&O, and CSX, alleged civil RICO violations and breach of state law fiduciary duty. The district court dismissed the action under Fed. R. Civ. P. 12(b)(6), concluding that the complaint alleged neither a sufficient pattern of racketeering activity to state a civil RICO claim nor sufficient fraud to state a claim for breach of fiduciary duty under state law. We affirm.

I

The facts alleged by the plaintiffs, which we must take as true for the purposes of ruling on this 12(b)(6) motion, are essentially as follows.

B&O is a Maryland railroad corporation in which the plaintiffs hold minority interests. Approximately 98.5% of the outstanding shares of B&O's common and

preferred stock is owned by C&O, a Virginia corporation. C&O in turn is a wholly-owned subsidiary of CSX Corporation, a Virginia holding company that owns a number of transportation, real estate, and mining concerns in the eastern seaboard region. Through its ownership of C&O, CSX dominates and controls the operations and financial affairs of B&O and its subsidiaries.

Prior to 1977, B&O owned substantial non-rail assets, including a large amount of potentially profitable real estate. CSX wished to develop these non-rail assets free from the claims of B&O's minority shareholders. To accomplish that goal, CSX in 1977 directed B&O to transfer virtually all its non-rail assets to its wholly-owned subsidiary, Mid-Allegheny Corp. (MAC). Following this transfer, CSX distributed the MAC stock to B&O's common shareholders as a dividend-in-kind, without giving advance notice of the proposed dividend to the holders of debentures convertible into B&O common stock. The effect of this transaction was to deprive the B&O debentureholders, who counted among their number the representative plaintiffs, of the opportunity to convert before the record date and thereby to share in the anticipated profits from the development of B&O's non-rail assets.[1]

[1] The plaintiffs also allege that between 1961 and 1978, CSX and C&O tricked large numbers of B&O debentureholders into selling their debentures to B&O at less than face value, by directing B&O not to pay dividends on its common stock.

Over the next several years, CSX transferred most of MAC's non-rail assets to other CSX affiliates. Between 1978 and 1979, CSX directed MAC's board of directors, which it controlled, to approve the sale of much of MAC's real estate to other CSX affiliates, allegedly at prices below fair value. In February 1983, CSX directed MAC's board of directors to approve the sale of MAC's controlling interest in the Western Maryland Co. (WMC), a profitable timber and mineral leasing concern, to another wholly-owned subsidiary of CSX, CSX Minerals, Inc. (CSX-M). This sale was also allegedly at a price below fair value. CSX then carried out a merger of WMC into CSX-M, and in connection with this merger, sent WMC's shareholders a proxy statement which allegedly contained various fraudulent misrepresentations and omissions.

CSX then began to spin off B&O's rail assets. In February 1983, it directed B&O's board of directors, which it controlled, to approve the sale of B&O's controlling interest in the Western Maryland Railroad Company (WMR) to B&O's parent, C&O, at a price allegedly below fair value. Following the sale, CSX engineered a merger of WMR into C&O and, in connection with this merger, mailed WMR's shareholders a proxy statement which allegedly contained various misrepresentations and omissions. CSX also endeavored to depress B&O's earnings, by shifting certain costs incurred in other CSX subsidiaries to it.

Finally, CSX proposed to rid itself of B&O's minority shareholders altogether by merging B&O into its parent corporation, C&O. It is this proposed merger which the plaintiffs, whose interests it would cash out, challenge in

this action. Because C&O owned more than 90% of the outstanding common stock of B&O, CSX was able to carry out the merger without securing shareholder approval, under Md. Corps. & Ass'ns Code Ann. §3-106. In connection with the merger, the plaintiffs allege that CSX made several false representations as to the value of B&O's assets, in order to induce them to accept less than the fair value of their stock as a cash-out price.

Shortly after the proposed merger was announced, the plaintiff minority shareholders filed actions against B&O, C&O, and CSX in both state and federal court. The state court complaint alleged essentially that the merger had no proper business purpose, that the price offered for the minority shares was grossly inadequate, and that C&O and CSX had breached the fiduciary duty they owed B&O's minority shareholders, as holders of the majority interest in B&O, by engaging in "unfair dealing, coercion, deception, manipulation, and gross and palpable overreaching tantamount to fraud." The complaint sought both injunctive relief against the merger and damages for the losses allegedly suffered by the plaintiffs as a result of it.

The amended federal complaint, which is the subject of this appeal, contains three counts. The first two counts attempt to state civil RICO claims under 18 U.S.C. §§1962(c) and 1962(a). Both counts are based on allegations that the defendants conceived an elaborate scheme to deprive B&O's minority shareholders of their right to participate in the profits from B&O's growth through a series of complex corporate transactions spanning more than a decade, that they committed numerous acts of mail fraud in furtherance of this

scheme, and that these acts constitute a "pattern of racketeering activity" under 18 U.S.C. §1961. The third count attempts to state a claim against C&O and CSX for breach of fiduciary duty under state law. Like its state counterpart, the federal complaint seeks both injunctive relief against the merger and damages based on it.

In early April 1987, the state court denied the plaintiffs' request for injunctive relief against the merger, finding the dispute to be essentially one over the value of the minority stock, which could adequately be dealt with in the statutory appraisal proceeding. The plaintiffs moved for leave to file an amended complaint setting out the allegations of fraud in greater detail. The state court denied this motion. The plaintiffs appealed to the Maryland Court of Special Appeals, which affirmed the denial of leave to amend, finding that even with the proposed amendments, the complaint failed to state a claim for relief under state law. Further appeal is now pending within the state court system.

On April 30, 1987, the merger was consummated, mooting the plaintiffs' request for prospective injunctive relief in this action. Shortly thereafter, the district court dismissed the federal action for failure to state a claim. The court reasoned that the first two counts of the amended complaint failed to allege a sufficient pattern of racketeering activity to state a civil RICO claim, and that the third count failed to allege the sort of fraud necessary to support a claim for breach of fiduciary duty under state law. This appeal followed.

II

18 U.S.C. §1964 enables a private plaintiff to bring a civil action for treble damages based on a violation of §1962. In this case, the plaintiffs' complaint attempts to assert civil RICO claims under both §1962(c) and §1962(a). A crucial element of the claim under both sections is the existence of a "pattern of racketeering activity." The district court held that neither of the RICO counts here alleged a legally sufficient pattern of racketeering activity and dismissed on that ground. We agree.[2]

The RICO statute defines a "pattern of racketeering activity" simply as "at least two" acts of racketeering activity within ten years of each other. 18 U.S.C. §1961(5). Our current interpretation of this rather sparse statutory definition has its genesis in the Supreme Court's decision in *Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479 (1985). There the Court rebuffed a movement

[2] On appeal, the defendants argue that the dismissal of the civil RICO counts may also be upheld on several other grounds not reached by the district court: (1) failure to allege with sufficient particularity at least two predicate acts of racketeering activity; (2) failure to allege an "enterprise" separate and distinct from the "persons" who committed the alleged RICO violations; (3) failure to allege an adequate nexus between the persons, the enterprise, and the alleged pattern of racketeering activity; (4) failure to allege injury to business or property as a result of the alleged RICO violations; and (5) that the plaintiffs, as individual shareholders, lack standing to sue because any injuries they suffered were merely derivative of the injury to the corporation itself. Because we agree with the district court that the allegations in the complaint, even if true, would fail to establish a pattern of racketeering activity, we do not address the other grounds for dismissal advanced by the defendants.

then afoot in the lower courts to limit the scope of the civil RICO provisions by reading in restrictions that do not appear on the face of the statute, such as a requirement that the plaintiff have suffered a special "racketeering injury." At the same time, however, the Court suggested that lower courts might properly curb the abuse of civil RICO by more careful delineation of the "pattern" requirement. *Id.* at 500. Exploring the pattern concept in dicta, the Court suggested that while two acts of racketeering activity are necessary to form a pattern, they are generally not sufficient. *Id.* at 496 n.14. Because the legislative history indicates that RICO was not meant to target "sporadic" or "isolated" instances of racketeering activity, the Court said, predicate acts constitute a pattern only when they reflect both "continuity" and "relationship." *Id.*, quoting S. Rep. No. 617, 91st Cong., 1st Sess. 158 (1969).

Since *Sedima*, the lower courts have struggled to give content to the vague notions of "continuity" and "relationship" that are now considered the distinctive characteristics of the RICO pattern." As the Seventh Circuit has remarked, *see, e.g., Morgan v. Bank of Waukegan*, 804 F.2d 970, 975 (7th Cir. 1986), this task has not been an easy one, for the terms "relationship" and "continuity," as used in *Sedima*, are inherently contradictory. "Relationship" implies that the predicate acts were committed close together in time, involve the same victim or type of misconduct, or both; "continuity" implies more extended periods of time almost inevitably involving different victims. *Id.* An excessive focus on either factor in a given fact situation may effectively eliminate the other. *Id.*

Recognizing this conceptual tension, we held in *International Data Bank v. Zepkin*, 812 F.2d 149 (4th Cir. 1987), that the existence of a RICO pattern must be determined on a case-by-case basis, rather than by reference to any set of mechanical rules. *Id.* at 154-55. Under this flexible standard, what constitutes a RICO pattern is thus "a matter of criminal dimension and degree," to be dealt with by reference to the facts and circumstances of each particular case. *Id.* at 155.

As *Zepkin* and the cases following it illustrate, it is the continuity aspect of *Sedima's* pattern analysis which has given us the greatest difficulty in application. We are not alone in this regard—the proper application of the continuity prong has bitterly divided the circuits. The Eighth Circuit has held that the continuity necessary to establish a pattern is not present when the predicate acts alleged were all committed in furtherance of a single continuing scheme. *See, e.g., Superior Oil Co. v. Fulmer*, 785 F.2d 252, 257 (8th Cir. 1986). The Second and Eleventh Circuits, by contrast, have focused solely on the number of related predicate acts, without regard to the existence of separate "schemes." *See, e.g., United States v. Ianniello*, 808 F.2d 184, 189-93 (2d Cir. 1986); *Bank of America v. Touche Ross & Co.*, 782 F.2d 966, 970-71 (11th Cir. 1986). The Seventh Circuit has taken a middle stance, holding that related predicate acts may reflect sufficient continuity to establish a pattern, even if they can be characterized as part of a single scheme, if they are "ongoing over an identified period of time so that they can fairly be viewed as constituting separate transactions, i.e., 'transactions "somewhat separated in

time and place." ' " *Morgan*, 804 F.2d at 975 (quoting *Graham v. Slaughter*, 624 F. Supp. 222, 225 (N.D. Ill. 1985) (quoting *United States v. Moeller*, 402 F. Supp. 49, 57-58 (D. Conn. 1975))). In making this determination, the Seventh Circuit has looked to the number and variety of the predicate acts and the length of time over which they were committed, the number of victims, the presence of separate schemes, and the occurrence of distinct injuries. *Id.*

In *Zepkin*, we adopted a flexible approach to the continuity inquiry not unlike that enunciated by the Seventh Circuit in *Morgan*. We agreed that the mere fact that the predicate acts alleged can properly be characterized as part of a single ongoing "scheme" should not automatically prevent them from constituting a pattern. 812 F.2d at 155. On the other hand, we recognized that a "single, limited scheme" designed to perpetrate a single fraud should not be transformed into a RICO violation simply because the fraud's commission required several acts of mail or wire fraud; such an interpretation would, we thought, virtually read the pattern requirement out of the statute, for it is "the unusual fraud that does not enlist the mails and wires in its service at least twice." *Id.* at 154-55. We did not attempt to identify a range of factors relevant to the continuity inquiry, as had the Seventh Circuit in *Morgan*. But we did indicate that the inquiry ought to focus on whether the related predicate acts suggested "ongoing unlawful activities whose scope and persistence pose a special threat to social well-being." *Id.* at 155.

Appendix C—Opinion of the United States Court of Appeals for the Fourth Circuit (1988).

The complaint in *Zepkin* alleged that the defendants had committed multiple acts of securities fraud by issuing a misleading prospectus to ten inventors in connection with a single stock offering. We found this insufficient to satisfy the continuity aspect of the pattern requirement because the predicate acts alleged were all designed to perpetrate a single fraud. *Id.* at 154-55. As we later explained, the multiplicity of the predicate acts in *Zepkin* was more a reflection of the nature of the underlying transaction—a securities deal which produced numerous pieces of paper—than of the scope and persistence of the criminal activity involved. *See HMK Corp. v. Walsey,* 828 F.2d 1071, 1974 (4th Cir. 1987) (quoting *Morgan,* 804 F.2d at 976). Predicate acts must be viewed in context, we stressed; the mere fact that a particular transaction generates numerous pieces of paper—and hence the potential for a greater number of related predicate acts—does not necessarily mean that those predicate acts in combination pose a special threat to social well-being. *Id.; see Morgan,* 804 F.2d at 976.

In *HMK Corp. v. Walsey,* 828 F.2d 1071 (4th Cir. 1987), we took the analysis a step further. There the complaint alleged that the developer defendants had made a series of misrepresentations to government officials in order to influence zoning decisions regarding a certain tract of land. Unlike the predicate acts in *Zepkin,* which occurred close together in time and were related to a single transaction, these predicate acts spanned a period of four years and could be grouped into several distinct "episodes" of activity somewhat separated in time and space. For this reason, the plaintiffs argued that the predicate acts reflected the

continuity necessary to make out a pattern. In rejecting this argument, we again emphasized the importance of context. On the facts of that case, we thought both the number of predicate acts and the length of time they spanned to be more a reflection of the peculiar context in which they had occurred—a protracted zoning dispute that required the involvement of many different governmental decisionmakers—than of criminal activity that posed a special threat to social well-being. *Id.* at 1074-76. We emphasized that the determination of whether particular predicate acts reflect "continuous" criminal activity cannot be made in a vacuum, but must take into account the inherent characteristics of the situation in issue. *Id.* at 1075.

This case presents the closest question yet, for the predicate acts alleged here span a period of ten years and can be grouped into several distinct "episodes" of activity, each of which is arguably self-contained. Indeed, the plaintiffs contend that these different "episodes" of fraudulent activity reflect the existence of at least four separate and distinct "schemes." The first such "scheme" is said to involve the 1977 transfer of B&O's non-rail assets to MAC and the subsequent declaration of the dividend in MAC stock without advance notice to the B&O debentureholders. The second and third "schemes" involve the 1983 freezeouts of the minority shareholders in two B&O subsidiaries, WMR and WMC; the fourth centers around the current effort to freeze out the minority shareholders in B&O itself. *See* Appellant's Brief at 5-7. The plaintiffs contend that the existence of these separate "schemes" demonstrates the continuity necessary to make out a RICO pattern.

Appendix C—Opinion of the United States Court of Appeals for the Fourth Circuit (1988).

We disagree. Even assuming that the allegations made here are legally sufficient to plead multiple acts of mail fraud—an issue we do not decide—we are not persuaded that the conduct thus alleged reveals sufficient continuity to establish a pattern, as that concept has been worked out in our cases. As the district court noted—and the plaintiffs' own complaint asserts repeatedly[3]—each of these allegedly separate "schemes" or "episodes" of fraudulent activity was merely another step toward the accomplishment of a single, limited goal: getting rid of the outside minority interests in B&O. There was in reality but a single "scheme" to inflict a single basic injury. Here, as in *HMK*, the number of predicate acts and the length of time over which they occurred are more a reflection of the peculiar context in which the activity occurred—a lengthy and bitter battle for control of a large corporate entity—than of ongoing criminal conduct whose scope and persistence poses a special threat to social well-being. Virtually every action taken by a controlling majority in the course of its stewardship of a corporation is subject to challenge as either mail or securities fraud. To hold indiscriminately that proof of several such acts occurring over the course of a period of years constitutes a RICO pattern would be to make the statute's extraordinary penalties available to virtually every disgruntled minority shareholder harmed in the process. Such a result would not only have a chilling effect on the transaction of legitimate corporate business, but also sanction a use of the RICO statute that we do not think Congress intended.

---

[3] See Joint Appendix 3A-4A; 7A; 35A.

We do not, of course, mean to suggest that a single ongoing scheme of racketeering activity can never constitute a pattern when it occurs in the corporate context. Indeed, one of the most obvious examples of a RICO pattern—a scheme that involves setting up a series of shell corporations, selling stock in them by means of various false representations, and then disappearing with the proceeds—occurs in the corporate context. Such an open-ended scheme contemplating the repeated infliction of independent economic injuries on an indiscrimnate number of victims may well pose a special threat to social well-being. We hold only that this *particular* scheme, limited in scope to the accomplishment of a single discrete objective—forcing out the minority in a single corporate structure—does not pose a sufficient threat of continuing criminal activity to justify imposition of RICO's extraordinary penalties. Though the activity engendered by this scheme was spread out over time, it was undertaken merely as a means to the accomplishment of that single end, and there is nothing to suggest that it would have continued for a moment longer than was necessary to accomplish it. Viewed in context, the separate acts emerge as no more deleterious than the multiple mailings in furtherance of the single discrete transaction in *Zepkin*. Such allegations of multiple preparatory acts leading up to the infliction of a single basic injury are simply not the stuff of which RICO patterns are made. *See*, e.g., finding similar allegations insufficient to meet *Sedima's* continuity requirement, *Medical Emergency Serv. Assoc. v. Foulke*, _____ F.2d _____ (7th Cir. Mar. 25, 1988) (multiple acts of mail fraud leading up to infliction of single injury, the displacement of plaintiff as

provider of emergency services); *Marks v. Pannell Kerr Forster,* 811 F.2d 1108, 1110-12 (7th Cir. 1987) (multiple fraudulent acts designed to inflict single injury on single victim); *Skycom Corp. v. Telstar Corp.,* 813 F.2d 810, 818 (7th Cir. 1987) (multiple fraudulent representations leading up to formation of single contract and transfer of single business opportunity); *Torwest DBC, Inc. v. Dick,* 810 F.2d 925, 928-29 (10th Cir. 1987) (allegations of multiple fraudulent acts designed to permit corporate insiders to recover illegal profits from sale of single piece of property); *Elliott v. Chicago Motor Club Ins.,* 809 F.2d 347, 349-50 (7th Cir. 1986) (multiple acts of mail fraud designed to defraud plaintiff in relation to single insurance claim); *see also Montesano v. Seafirst Comm. Corp.,* 818 F.2d 423, 426 (5th Cir. 1987) (Higginbotham, J.) (suggesting similar analysis).

We wish to emphasize that by focusing on the ultimate objective of the related predicate acts at issue, we are not holding that it is necessary to show more than one fraudulent "scheme" or criminal "episode" to establish a pattern. Such an approach is, in our judgment, utterly indefensible after *Sedima,* for the RICO statute itself contains no requirement of multiple "schemes" or "episodes." Nor do we mean to suggest that related predicate acts may always avoid RICO liability by the "semantical game of generalizing the[ir] illegal objective." *See Montesano,* 818 F.2d at 426. Quite plainly, a scheme that contemplates the repeated infliction of independent economic injuries—e.g., a series of bank robberies or embezzlements—should not escape characterization as a pattern simply because each

criminal act shares the same general objective—the robbing of banks or the embezzlement of funds. Schemes such as these, which involve the repeated infliction of independent economic injuries—and thus the reaping of independent illegal benefits—are precisely the sort of ongoing criminal activity to which *Sedima's* continuity requirement is addressed. *See, e.g., Liquid Air Corp. v. Rogers,* 834 F.2d 1297, 1303-05 (7th Cir. 1987) (allegations that defendants mailed 19 different false shipping invoices over period of seven months to document shipments that were never made were sufficient to satisfy continuity requirement, because each false invoice was a separate fraud resulting in an independent economic injury and concomitant illegal benefit); *Illinois Dept. of Revenue v. Phillips,* 771 F.2d 312, 313 (7th Cir. 1985) (allegations that defendant mailed nine separate fraudulent sales tax returns to the state over a nine-month period were sufficient to constitute pattern). We hold only that the objective of the related predicate acts is a factor to be considered in assessing the criminal dimension and degree. In this case, that objective is sufficiently limited that we cannot say the related predicate acts suggest ongoing criminal activity of sufficient scope and persistence to pose a special threat to social well-being.

III

We turn next to Count III of the amended complaint, which attempts to assert a claim for breach of fiduciary duty under state law. Under Maryland law, a minority shareholder who objects to the price offered him by the majority in a §3-106 merger may elect instead to receive

the fair value of his stock through the appraisal process set forth in Md. Corps. & Ass'ns Code Ann. §§3-201 to -213. Md. Corps. & Ass'ns Code Ann. §§3-106(d)(2). The statute itself does not indicate whether this appraisal proceeding is the exclusive remedy available to a dissenting minority shareholder in a §3-106 merger. Maryland's highest court has not specifically addressed this issue, but it has indicated that minority shareholders may, under certain circumstances, obtain equitable relief against similar "freezeout" maneuvers, notwithstanding the existence of the statutory appraisal remedy. *See Lerner v. Lerner,* 511 A.2d 501, 505-06 (Md. 1986); *Homer v. Crown Cork & Seal Co.,* 141 A. 425, 432 (Md. 1928); *see also Twenty Seven Trust v. Realty Growth Investors,* 533 F. Supp. 1028, 1034-36 (D. Md. 1982) (applying Maryland law). Drawing on these precedents, Maryland's intermediate appellate court has recently held that dissenting minority shareholders may, under certain limited circumstances, obtain equitable relief against a §3-106 freezeout merger, despite the existence of the statutory appraisal remedy. *Walter Schloss Assoc. v. The Chesapeake & Ohio Ry.,* No. 710, Sept. Term 1977, slip op. at 14-15 (Md. Ct. Spec. App. Jan. 20, 1988). While the *Schloss* decision is of course not binding on us, we think it represents the best available prediction of the position the Maryland Court of Appeals would likely take on the issue. We therefore assume, as did the district court, that Maryland law permits a dissenting minority shareholder to obtain equitable relief against a §3-106 freezeout merger, in certain circumstances.

Identifying the circumstances under which such relief is available, however, is a much more difficult task. In *Homer*, the Court of Appeals held that an allegation that the price offered for minority shares was "grossly inadequate" would not justify equitable relief because such a claim could be fairly resolved in the statutory appraisal proceeding. 141 A.2d at 432. Equitable relief was warranted, the court held, only where there was "fraud" on the part of the majority or the officers and directors it controlled. *Id.* But the *Homer* court recognized that allegations of "fraud" are often nothing more than disagreements about methods of valuation, which are more appropriately resolved in the statutory appraisal proceeding. It therefore directed courts to view allegations of fraud with suspicion and to deny equitable relief "if, on consideration of all the allegations of the bill of complaint, it appear[s] that the fundamental issue thus made is not fraud, but a debatable controversy over value." *Id.* To take the case out of the appraisal statute, the court held, the fraud must be "affirmatively shown." *Id.* Applying this careful scrutiny to the allegations of fraud in the complaint before it, the court found them to be in essence nothing more than a complaint about the method by which the value of the minority shares was calculated. Since this dispute could adequately be resolved in a statutory appraisal proceeding, the court found the allegations insufficient to state a claim for equitable relief. *Id.* at 433-34.

Homer was decided in 1928, and the general body of corporate law has changed a great deal in the intervening years. During the 1970s, many courts held that minority

shareholders could obtain equitable relief against freezeout mergers upon a showing that the merger had no legitimate "business purpose" other than to force out the minority. *See, e.g., Singer v. Magnavox Co.*, 380 A.2d 969, 980 (Del. 1977). In *Weinberger v. UPO, Inc.*, 457 A.2d 701 (Del. 1983), the Delaware Supreme Court abandoned this "no independent business purpose" rule and held that a minority shareholder could obtain equitable relief against a freezeout only upon a showing that the transaction did not meet the test of "entire fairness." "Entire fairness," said the Delaware court, meant both "fair dealing" and "fair price," *id.* at 711; for this reason, equitable relief might be appropriate not only in cases of actual fraud, but also where the majority had engaged in "misrepresentation, self-dealing, deliberate waste of corporate assets, or gross and palpable overreaching," *id.* at 714. It is this broad "fairness" exception to the exclusivity of the statutory appraisal remedy, rather than the narrow "actual fraud" exception recognized by the Maryland Court of Appeals in *Homer*, that the plaintiffs urge us to apply in juding the sufficiency of their complaint.

We decline to do so. Three years after *Weinberger*, the Maryland Court of Appeals was asked to adopt its "fairness" approach to minority freezeouts in an appeal from the grant of a preliminary injunction against such a merger. *See Lerner*, 511 A.2d at 511.[4] It specifically

[4] While the court was asked to do so by a majority shareholder who sought to avoid the business purpose doctrine, the court's discussion made clear that it was considering all aspects of the *Weinberger* rule. *See* 511 A.2d at 511.

declined to decide whether to do so, saying that such a decision involved "serious, substantial, difficult and doubtful" issues that would require "more deliberate investigation." *Id.* At the same time, the Court of Appeals specifically reaffirmed *Homer's* holding that equitable relief was not available to a minority shareholder when careful analysis of his complaint revealed it to be nothing more than a complaint about the adequacy of the price offered for his shares. *Id.* at 506. Because the *Weinberger* issue was presented to the Maryland court in the preliminary injunction context, its refusal to adopt that doctrine cannot be taken as an affirmative indication that it would not do so, upon further reflection. Absent more authoritative guidance from the state's highest court, however, it is not for this court, sitting in diversity, to extend state law in the manner suggested. Accordingly, it is *Homer's* actual fraud rule, rather than the *Weinberger* "general fairness" test, that we apply in judging the sufficiency of this complaint.

Viewing the plaintiffs' attempted allegations of "fraud" with the suspicion mandated by *Homer*, and under the stringent pleading requirement of Fed. R. Civ. P. 9(b), we are convinced, as was the district court, that they are not sufficient to state a claim for equitable relief under existing Maryland law. Paragraphs 55-70 contain various complaints about income and asset valuations and methods of accounting, which are, as indicated earlier, insufficient to warrant equitable relief under *Homer*. Paragraph 71 alleges that the defendants "concealed from the investing public material

information concerning B&O in order to manipulate and control the price ... of the B&O common stock." Specifically, paragraph 71a alleges that the defendants failed to disclose B&O's plans to sell one or more of its short-line railroads; paragraph 71b that they failed to disclose B&O's projections of income for 1986 and 1987, and that they waited until March of 1987 to disclose B&O's 1986 earnings, though the information was available in January. None of these allegations is sufficient to plead a case of fraud under Maryland law and Fed. R. Civ. P. 9(b), for all of this information was fully disclosed to the B&O shareholders in the notice of merger, and there are no specific facts alleged that show the failure to disclose it earlier affected the market price of B&O's stock or otherwise caused the plaintiffs injury.[5]

Paragraph 72 alleges that the defendants concealed until the merger was announced that Morgan Stanley, which CSX retained as an "independent financial advisor" to provide the appraisals of B&O's common stock used to calculate the cash-out price, had had previous business dealings with CSX, including underwriting CSX offerings and maintaining a trading position in CSX stock. But there is no specific allegation that these prior business dealings prevented Morgan Stanley from exercising independent business judgment in this case, and it is, in any event, undisputed that the prior dealings were fully disclosed to the minority

[5] The plaintiffs' conclusory allegations that the information concealed was relevant to the market's valuation of the B&O stock, see ¶71a, is insufficient to plead fraud under Rule 9(b).

shareholders in the notice of merger. These conclusory allegations of bias are simply insufficient to make out the concrete case of fraud required by *Homer*.

In sum, we think a fair reading of the complaint as a whole reveals the plaintiffs' fundamental grievance to be one of inadequate price, rather than fraudulent dealing. Because the statutory appraisal remedy provides a wholly adequate—and in these circumstances exclusive—remedy for price inadequacy, we agree with the district court that the third count of the complaint fails to state a claim upon which relief can be granted. We are bolstered in this conclusion by a recent decision of the Maryland Court of Special Appeals in the parallel state court litigation challenging this same merger. *See Walter J. Schloss Assoc. v. The Chesapeake & Ohio Ry.*, No. 710, Sept. Term 1977 (Md. Ct. Spec. App. Jan. 20, 1987). The plaintiffs in *Schloss* are represented by the same counsel as the plaintiffs in this case, and the allegations in their complaint are in all material respects the same as those in the complaint now before us.[*] The Maryland court found these allegations insufficient to state a claim for equitable relief under *Homer*, and we think the same analysis applies here.

IV

For the foregoing reasons, the judgment of dismissal is affirmed.

AFFIRMED.

---

[*] We have considered carefully the differences between the two complaints pointed out by the plaintiffs and find them to be inconsequential.

Appendix C—Opinion of the United States Court of Appeals for the Fourth Circuit (1988).

CERTIFICATE OF SERVICE

I hereby certify that on the 23rd day of September, 1988, a true and correct copy of the foregoing Petition for Certiorari was served by United States first-class mail, postage prepaid, addressed to:

Richard Magid, Esquire
WHITEFORD, TAYLOR & PRESTON
1400 Union Trust Tower
Suite 1400
7 St. Paul Street
Baltimore, MD 21202

MICHAEL P. MALAKOFF